

## Internal Revenue Service

Number: **201707007**

Release Date: 2/17/2017

Index Number: 1041.00-00, 2601.03-01,  
2041.03-00, 2514.00-00

Department of the Treasury  
Washington, DC 20224

Third Party Communication: None  
Date of Communication: Not Applicable

Person To Contact:

Telephone Number:

Refer Reply To:  
CC:PSI:B04  
PLR-116466-16

Date:  
October 31, 2016

### Legend

Husband  
Wife  
Date  
Year  
Company

a  
b

Dear :

This letter responds to your authorized representative's letter dated May 12, 2016, requesting income, gift, estate, and generation-skipping transfer (GST) tax rulings with respect to a transfer from a trust.

The facts and representations submitted are summarized as follows:

Husband and Wife were married on Date. Husband and Wife separated in Year, and later that year, Husband filed for divorce.

Husband and Wife negotiated a proposed settlement agreement regarding marital support obligations and property rights. The proposed settlement agreement provides for the establishment of a trust for the benefit of Wife. The trust will be initially funded with half of Husband's shares in Company. Wife will receive all of the net income of the trust annually. The trustee has the discretion to make distributions of principal to Wife, but is prohibited from distributing Company shares to her or from selling Company shares in order to make such principal distributions. In addition, when

the trust holds assets other than Company stock, Wife will have the right to withdraw the greater of \$a or b percent of the principal for the trust each year. Trust does not grant Wife any powers to appoint trust property either during her life or upon death. In exchange, Wife will relinquish all marital rights and property claims that she might have acquired while married to Husband. Upon Wife's death, the remaining trust principal will revert to Husband, or Husband's estate if Husband predeceases Wife. The proposed settlement agreement does not become final or binding upon Husband and Wife until the receipt of a favorable private letter ruling from the Internal Revenue Service.

You have requested the following rulings:

1. Husband will not recognize any income tax gain or loss upon the creation of the trust pursuant to § 1041.
2. Husband's transfer of the income interest in the trust to Wife will constitute a transfer for full and adequate consideration under § 2516 and will not be a gift by Husband.
3. Section 2702(a) will not apply to for purposes of determining whether Husband's transfer to Wife of the income interest in the trust is a gift or for purposes of determining the value of such transfer.
4. The fair market value of the trust property on Husband's date of death (or the alternate valuation date, as the case may be), reduced by the fair market value of Wife's outstanding income interest (determined in accordance with the valuation tables of § 20.2031-7), will be includible in Husband's gross estate upon his death under §§ 2036(a)(1) and 2036(a)(2).

## LAW AND ANALYSIS

### Ruling 1

Section 1001(a) provides that the gain from the "sale or disposition of property" is "the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain," and the loss is "the excess of the adjusted basis provided in such section for determining loss over the amount realized." Section 1001(c) provides that, except as otherwise provided, "the entire amount of the gain or loss, determined under this section, on the sale or exchange of property shall be recognized."

Section 1041(a) provides that no gain or loss shall be recognized on a transfer of property from an individual to (or in trust for the benefit of) (1) a spouse, or (2) a former spouse, but only if the transfer is incident to a divorce.

Section 1041(b) provides that, in the case of any transfer of property described in § 1041(a) the property shall be treated as acquired by the transferee by gift, and the basis of the transferee in the property shall be the adjusted basis of the transferor.

Section 1041(c) provides that for purposes of § 1041(a)(2) a transfer of property is incident to the divorce if the transfer occurs (1) within one year after the date on which the marriage ceases, or (2) is related to the cessation of the marriage.

Section 1.1041-1T(b) Q&A-7, of the Temporary Income Tax Regulations provides that a transfer of property is related to the cessation of the marriage if the transfer is pursuant to a divorce or separation instrument, as defined in § 71(b)(2) and the transfer occurs not more than six years after the date on which the marriage ceases. A divorce or separation instrument includes a modification or amendment to such decree or instrument.

Husband proposes to transfer Company shares to an irrevocable trust for the benefit of Wife. Under the terms of the trust, Wife will receive all net income from the trust during life and may, at the discretion of the trustee, receive distributions of principal. The trustee may not, however, distribute shares to Wife nor sell such shares in order to make cash distributions to Wife. At the death of Wife, any remaining trust principal will be distributed to Husband, or, should Husband predecease Wife, Husband's estate.

Husband will transfer the shares of Company to the trust within six years after the entry of the final judgment of divorce. In return, Wife will relinquish all marital rights and property claims that she acquired while married to Husband. This arrangement is to be formalized in a legally binding property settlement agreement between Husband and Wife prior to the transfer of Company shares to the trust.

Accordingly, based on the facts submitted and representations made, provided that the transfer of Company shares to the trust occurs within six years of the entry of final judgment of divorce and the terms of the trust and the proposed settlement agreement as executed by Husband and Wife remain materially identical to those submitted as part of Husband's ruling request, we conclude that Husband will not recognize gain or loss on the transfer of Company shares to the trust.

## Ruling 2

Section 2501(a)(1) imposes a tax for each calendar year on the transfer of property by gift during the calendar year by any individual.

Section 2511(a) provides that the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2512(b) provides that where property is transferred for less than an adequate and full consideration in money or money's worth, the amount by which the value of the property exceeds the value of the consideration shall be deemed a gift.

Section 2516 provides that where a husband and wife enter into a written agreement relative to their marital and property rights and divorce occurs within the three-year period beginning on the date one year before the agreement is entered into (whether or not the agreement is approved by the divorce decree), any transfers of property or interests in property made pursuant to the agreement (1) to either spouse in settlement of his or her marital or property rights, or (2) to provide a reasonable allowance for the support of issue of the marriage during minority, shall be deemed to be transfers made for a full and adequate consideration in money or money's worth.

In this case, Husband and Wife entered into a proposed settlement agreement relative to their marital support and property rights in contemplation of divorce. Under the terms of the settlement agreement, Husband will transfer one-half of Husband's shares of Company stock to Trust in exchange for Wife's relinquishment of her marital support and property rights. Under the terms of Trust, Wife has the right to receive the income for life, the right to discretionary distributions of principal (excluding distributions of Company stock) and, if the trust holds assets other than Company stock, the annual right to withdraw the greater of \$a or b percent of the value of Trust from trust principal.

Accordingly, based on the facts submitted and representations made, we conclude that, assuming a final judgment of divorce occurs within the three-year period beginning on the date one-year before the agreement is entered into, Husband's transfer to the trust will constitute a transfer for full and adequate consideration under § 2516, and will not be considered a taxable gift by Husband to anyone.

### Ruling 3

Section 2702(a)(1) provides that solely for purposes of determining whether a transfer in trust to (or for the benefit of) a member of the transferor's family is a gift (and the value of such transfer), the value of any interest in such trust retained by the transferor or by any applicable member of the transferor's family (as defined in § 2701(e)(2)) shall be determined as provided in paragraph (2).

Section 2702(a)(2)(A) provides that the value of any retained interest which is not a qualified interest shall be treated as zero.

Section 25.2702-2(a)(3) of the Gift Tax Regulations provides that the term “retained” means held by the same individual both before and after the transfer in trust. In the case of the creation of a term interest, any interest in the property held by the transferor immediately after the transfer is treated as held both before and after the transfer.

Section 2702(e) provides that the term “member of the family” has the meaning given such term by § 2704(c)(2). Section 2704(c)(2) defines “member of the family” to mean, with respect to an individual, (A) such individual’s spouse, (B) any ancestor or lineal descendant of such individual or such individual’s spouse, (C) any brother or sister of the individual, and (D) any spouse of any individual described in clause (B) or (C).

Section 2702(c)(1) provides that for purposes of this section, the transfer of an interest in property with respect to which there is one or more term interests shall be treated as a transfer of an interest in trust. Section 2702(c)(3) provides that the term “term interest” means either a life interest in property, or an interest in property for a term of years.

Section 2702(a)(3)(A)(iii) provides that § 2702(a) shall not apply to any transfer to the extent that regulations provide that such transfer is not inconsistent with the purposes of this section.

Section 25.2702-1(c)(7) provides that § 2702 does not apply to a transfer in trust if the transfer of an interest to a spouse is deemed to be for full and adequate consideration by reason of § 2516 (relating to certain property settlements) and the remaining interests in the trust are retained by the other spouse.

Section 25.2702-4(d), Example 5, considers a situation where H and W enter into a written agreement relative to their marital and property rights that requires W to transfer property to an irrevocable trust, the terms of which provide that the income of the trust will be paid to H for 10 years. On the expiration of the 10-year term, the trust is to terminate and the trust corpus is to be paid to W. H and W divorce within two years after the agreement is entered into. Pursuant to § 2516 the transfer to H would otherwise be deemed to be for full and adequate consideration. Section 2702 does not apply to the acquisition of the term interest by H because no member of H's family acquired an interest in the property in the same transaction or series of transactions. The result would not be the same if, on the termination of H's interest in the trust, the trust corpus were distributable to the children of H and W rather than W.

In this case, under the terms of the proposed settlement agreement, Husband is transferring property to the trust in exchange for Wife’s relinquishment of her marital support and property rights. As mentioned above, the transfer of the property to Trust is

deemed to be for full and adequate consideration under § 2516 Husband will retain the entire remainder interest in Trust by reason of the reversion. Accordingly, based on the facts submitted and representations made, we conclude that § 2702(a) will not apply for purposes of determining whether Husband's transfer to Wife of the term interest in the trust is a gift or for purposes of determining the value of such transfer.

#### Ruling 4

Section 2031(a) provides that the value of the gross estate of the decedent shall be determined by including to the extent provided for in this part, the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated.

Section 2033 provides that the value of the gross estate shall include the value of all property to the extent of the interest therein of the decedent at the time of his death.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in a case of a bona fide sale for adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period that does not in fact end before his death (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 20.2036-1(b)(1)(ii) of the Estate Tax Regulations provides, in relevant part, that a reservation by the decedent "for any period not ascertainable without reference to his death" includes a situation where a decedent reserved the right to receive the income, annuity, or other payment from transferred property after the death of another person who was in fact enjoying the income, annuity, or other payment at the time of the decedent's death. In such case, the amount to be included in the decedent's gross estate under § 2036(a)(1) does not include the value of the outstanding interest of the other person.

Section 20.2036-1(c)(1)(i) provides that if the decedent retained or reserved an interest or right with respect to all of the property transferred by him, the amount to be included in the gross estate under § 2036 is the value of the entire property, less only the value of any outstanding income interest which is not subject to the decedent's interest or right and which is actually being enjoyed by another person at the time of the decedent's death.

Section 20.2031-7 provides information to calculate the present value of certain interests that are dependent upon life or a term of years.

In this case, the trust provides that upon Wife's death, the remaining trust principal will revert to Husband, or to Husband's estate if Husband predeceases Wife. Under § 2036(a)(1) the value of property that a decedent has transferred into trust will be includible in that decedent's estate if he has retained the possession or enjoyment of, or the right to the income from, the property for any period not ascertainable without reference to his death. In this case, Husband retained the right to the trust property if he survives Wife. Therefore, if Husband survives Wife, § 2036(a)(1) will apply to require inclusion of the trust property in Husband's gross estate. Under § 2036(a)(2) the value of property that a decedent has transferred into trust will be includible in that decedent's gross estate where he has retained the right, alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or income therefrom. In this case, Husband retained the prescribed power over the trust property for his life. Therefore, if Husband predeceases Wife, § 2036(a)(2) will apply to require inclusion of the trust property in Husband's gross estate. Under § 2036(a)(1) or 2036(a)(2) the value of the trust property included in Husband's gross estate is reduced by the value of Wife's outstanding income interest (determined in accordance with the valuation tables prescribed in § 20.2031-7).

Accordingly, based on the facts submitted and representations made, we conclude that the fair market value of the trust property on Husband's date of death (or the alternate valuation date, as the case may be), reduced by the fair market value of Wife's outstanding term interest (determined in accordance with the valuation tables of § 20.2031-7), will be includible in Husband's gross estate upon his death under §§ 2036(a)(1) and 2036(a)(2).

In accordance with the Power of Attorney on file with this office, we have sent a copy of this letter to your authorized representatives.

Except as expressly provided herein, we neither express nor imply any opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the Taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Lorraine E. Gardner

Lorraine E. Gardner  
Senior Counsel, Branch 4  
Office of the Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures

Copy for § 6110 purposes  
Copy of this letter

cc: